Drivers in place, auto component makers cruise

India's auto components industry will clock healthy growth steered by product changes (replacing metal with plastic/high-grad and lighter metals, increasing electronic content) and regulations (emission and safety norms).

Emerging technologies such as automated manual transmission, anti-lock braking systems, electronic control units/sensors, and advanced engine designs will be highlights. Further, with safety becoming the main concern, requirement for advanced driver assistance systems for lane assistance, distance control, and vehicle-to-vehicle communication, is on the rise.

In fiscal 2019, CRISIL Research expects the auto components industry to grow 12-14% on-year over a high base, on the back of demand from domestic manufacturers across vehicle segments. Led by improved rural demand (assuming normal monsoon) and state pay commission pay-outs, we expect the demand for two-wheeler and passenger vehicle segments to remain buoyant. Higher sourcing is expected from commercial vehicle (CV) and tractor manufacturers, who have been benefiting from the government's infrastructure push and four consecutive years of good crops.

Exports – the bulk of which is to the US and the euro zone – are expected to rise 8-10% on-year given firm global automobile demand. Exports will also improve to countries in South-east Asia and Latin America, primarily Brazil as it recovers from recession.

Several Japanese and Indian manufacturers have started sourcing components from India because of cost competitiveness owing to economies of scale. Northward trend of crude oil prices signals improvement in the Middle East economy as well. However, global trade and geo-political issues remain key monitorables. However, exports in fiscal 2019 will marginally be lower than the previous fiscal due to capacity constraints faced by auto component players as they are increasingly focussing on the domestic market.

Domestic demand on a canter

Segments	FY17	FY18E	FY19P
OEM	10%	14%	14-16%
Replacement	8%	7-9%	7-9%
Exports	1%	9-11%	8-10%
Imports	3%	9-11%	7-9%

E: Estimated; P: Projected

Source: CRISIL Research

In fiscal 2018, original equipment manufacturer (OEM) offtake grew by 14% on-year driven by the growth in two-wheelers because of improving rural sentiment; passenger vehicles due to increasing affordability, easier access to finance and various model launches; and CVs because of improvement in freight demand. Exports are estimated to have grown 9-11% mainly on account of the improving global economic scenario. In major export destinations, such as the US, auto sales, mainly Class 8 trucks, grew by greater than 70% in 2017. Another major economy, Europe has also shown signs of revival. Auto component exports to other emerging economies such as South-east Asia and Latin America have also shown substantial growth.

Further, the transition from Bharat Stage (BS)-III to BS-IV norms led to higher average realisation, particularly for CV component manufacturers, in fiscal 2018.

EBITDA margin to contract marginally in fiscal 2018, be stable in fiscal 2019

Raw material costs of auto component manufacturers bottomed out in fiscal 2016 and began to rise in fiscal 2017, putting pressure on the gross margin. The auto raw material index started rising ~13% on-year from the second quarter of fiscal 2017. With the index estimated to have risen a further 7% on-year in fiscal 2018, margins are estimated to have crimped 40-60 basis points on-year to 13.3-13.5% for 107 companies, which comprise 35% share of the industry. In fiscal 2019, EBITDA margin is projected to be stable at 13.3-13.5% as cost optimisation measures by manufacturers negate an expected 1-3% marginal rise in the raw material index.

Capital expenditure to rise owing to tighter regulations

Auto component makers are estimated to have incurred higher on-year capital expenditure for a couple of years from fiscal 2018 on account of the government's decision to implement BS-VI norms from fiscal 2021. Many players are also investing in new technology to capitalise on the rising demand for hybrid and electric vehicles.

Debt protection metrics to remain healthy despite capital investments

The industry's debt protection metrics are forecast to remain comfortable despite the capital expenditure as CRISIL Research projects healthy cash flows because of the acceleration in vehicle demand.

Long-term prospects better than near-term outlook

Domestic auto component production is projected to increase at 10-12% CAGR between fiscals 2018 and 2023 to ~Rs 5,223 billion, in line with the domestic automobile demand and exports. Demand from OEMs is expected to rise 11-13% CAGR, and exports by 10-12% CAGR. Localisation drive by OEMs and deeper penetration of components in a vehicle to comply with various safety and emission norms will boost the demand for auto components.

Auto-component exports are forecast to rise as India is well-position as a hub for global OEMs due to its cost competitiveness, auto component exports are forecast to rise at 10-12% between fiscal 2018 and 2023. We expect imports to grow at a moderate pace of 6-8% CAGR till fiscal 2023 to support domestic demand despite the higher anti-dumping duty levied on various engine, electrical and chassis parts under Union Budget 2018-19. In the long term, transfer of technology through collaboration with foreign players and localisation efforts will keep imports in check.

However, in fiscal 2021, auto component offtake is expected to slow down on-year as implementation of BS-VI norms will sharply increase prices and, consequently, lower automobile demand.

On a smooth long drive

Segments	FY13 - FY18E	FY18 - FY23P
OEM	7%	11-13%
Replacement	6-8%	6-8%
Exports	7-9%	10-12%
Imports	4-6%	6-8%

Source: CRISIL Research

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